APPENDIX

UNITED STATES COURT OF APPEALS
For the Seventh Circuit
Chicago, Illinois 60604

Submitted: October 3, 1974
October 11, 1974

Before
Hon. LUTHER M. SWYGERT, *Chief Judge*
Hon. THOMAS E. FAIRCHILD, *Circuit Judge*
Hon. WILBUR F. PELL, JR., *Circuit Judge*

HAROLD O'BRIEN, et al.,
Plaintiffs-Appellees,

vs.

Nos. 74-1671, 74-1672
74-1673, 74-1674
74-1675, 74-1683

CONTINENTAL ILLINOIS NATIONAL BANK AND TRUST COMPANY OF CHICAGO,
Defendant-Appellant.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

Nos. 72-C-660, 73-C-3132, 72-C-2935, 73-C-772 and 73-C-46

Frank J. McGarr, Judge.

ORDER

This matter comes before the Court on the motion of plaintiffs-appellees in the above-entitled appeals for dismissal thereof and upon the response of defendant-appellant thereto.

Upon consideration thereof, It Is Ordered that the Clerk of this Court enter judgment dismissing the appeals above-named on the ground that the orders appealed from are not final or otherwise appealable.

Local 734 Bakery Drivers Pension Fund Trust, et al. v. Continental Illinois National Bank and Trust Company of Chicago.

United States District Court, Northern District of Illinois, Eastern Division. Nos. 72 C 2551, 72 C 2935, 73 C 46, 73 C 660, and 73 C 772. May 10, 1974.

McGARR, District Judge:

I.

The five cases before this Court allege violations of Section 10(b) and Rule 10b-5 of the Securities Exchange Act of 1934, 15 U. S. C. § 78(j) and common law claims for breach of fiduciary obligations and contract. Jurisdiction is based on 15 U. S. C. § 78(aa) for the Federal claims and pendent jurisdiction is asserted as to the state-law claims. Additionally, in Cause No. 73 C 772, the plaintiff alleges violations of § 17(a) of the Securities Act of 1933, 15 U. S. C. § 77(q), and bases jurisdiction on 15 U. S. C. § 77(u). Besides the claim of pendent jurisdiction, diversity of citizenship (28 U. S. C. § 1332) is alleged to exist as to the state claims in this latter case.

Currently pending before this Court are the following motions:

1. Motions to dismiss all these cases for various reasons, including failure to state a claim upon which relief may be granted, lack of Federal jurisdiction, lack of capacity to sue and improper party plaintiff.

2. A motion to dismiss Counts I, III and V in Cause No. 73 C 772, which counts are brought under Section 17(a) of the 1933 Act, 15 U. S. C. § 17(q)(a).

3. A motion to dismiss Counts 9 through 13 in Cause No. 73 C 660 for lack of diversity of citizenship jurisdiction (28 U. S. C. § 1332).

4. A motion to dismiss Counts V and VIII of Cause No. 73 C 660 for lack of jurisdiction over the subject matter, and for failure to state a claim upon which relief can be granted.

The allegations of the five complaints, each with several plaintiffs, are sufficiently similar that the issues raised and the principles of law involved are generally the same for all.

It should be noted here that no leave has yet been granted to any plaintiff to proceed on behalf of a class. The class action determination is expressly reserved for later consideration.

No. 72 C 2551

Plaintiffs in this case are the trustees of Local 734 Bakery Drivers Pension Fund Trust ("Bakery Drivers"), the trustees of the Chicago District Council of Carpenters Pension Fund ("Carpenters"), the Trustees of The Chicago Area Retail Food Clerks Pension Fund ("Food Clerks"), the trustees of the Roofers' Pension Fund ("Roofers"), and the members of the Retirement Allowance Committee of the Chicago Transit Authority Retirement Plan ("CTA"). Plaintiffs also seek to bring this as a class action on behalf of all persons for whose trust or agency accounts the Bank purchased, sold or retained the named common stock without disclosing certain material information.

The plaintiffs allege that the Bank entered into a variety of relationships with the various plaintiffs, all of whom granted the Bank the discretion to purchase and sell securities on their behalf. They allege agreements with Food Clerks and with the Carpenters whereby the Bank agreed to act as agent for the investment of the pension funds, corporate trust agreements with the Drivers and the Roofers; and a retirement plan trust agreement with the CTA. Between February 1, 1968 and December 23, 1968, the Bank purchased, pursuant to its various agreements, 21,600 shares of Penn Central Company common stock, at a cost of approximately $1,250,000. It is alleged in Count I of the complaint that at the time of, or prior to, the purchases, Continental Bank had loaned substantial funds to Penn Central and had available to it detailed inside information with respect to the financial condition of Penn Central; that it failed to dis-

close to the plaintiffs that there existed a conflict of interest due to the Bank's dual position and that the Bank might be prohibited as an insider from trading in Penn Central stock. The plaintiffs further allege that due to this failure to inform them, they were induced to acquiesce in the purchases and to continue their relationship with and reliance upon the Bank. In June, 1970, shortly before Penn Central filed a petition in bankruptcy, the stock was sold with a resultant aggregate loss to the plaintiffs of approximately $1,000,000.

In Count II, the plaintiffs allege that the detailed information available to the Bank was used to make a complete financial analysis of Penn Central; that at the time of the purchases and up to the public announcement of Penn Central's petition in bankruptcy, the Bank knew and failed to disclose that Penn Central's stock was not of suitable investment quality and that Penn Central could not meet its working capital, debt service or dividend requirements, that it had accelerating losses and that the market price of its common stock was inflated. Count III alleges that Continental knew and failed to disclose the true financial status of Penn Central, that it delayed in selling the shares until shortly before or after the petition in bankruptcy and that the non-disclosure induced the plaintiffs to acquiesce in these matters. Count IV alleges that the Bank's interests were in continuous conflict with the plaintiff's and that it failed to sell the stock in order to protect its own interests. The remaining counts (5 through 8) are based upon breaches of contractual and fiduciary duties.

No. 72 C 2935

This eight-count complaint is brought by the trustees of the Chicago District Council of Carpenters Pension Fund ("Carpenters"). Pursuant to an agreement with the trustees, the Bank was appointed as agent with authority to invest in securities according to its discretion. The Carpenters claim that they lost $140,488.50 on the sale of 6,000 shares of common stock

issued by Management Assistance, Inc. ("MAI"), a corporation of which the Bank was the principal creditor. The remaining allegations set out basically the same claims as presented in 72 C 2551, the first four counts alleging violations of Section 10(b) of the Exchange Act and Rule 10b-5 and the latter four counts alleging breaches of contract and fiduciary duties by the Bank.

No. 73 C 46

This case was brought by the trustees of the Chicago Hotel Employees Pension Trust Fund ("Hotel Employees"), the trustees of the General Service Employees' Local Union No. 73 Employees' Pension Fund ("Service Employees"), the trustees of the Licensed Tugmen's and Pilots' Pension Fund ("Tugmen"), and the Trustees of the Dairy Employees'—Milk Dealers' Pension Plan Trust ("Dairy Employees"). Pursuant to trust agreements entered into with the plaintiff-trustees which granted it investment discretion, the Bank "bought" units of Continental Illinois Investment Trust for Employee Benefit Plans ("CIIT"). CIIT is a trust established under the laws of the State of Illinois with the Bank as trustee and consists of the commingled assets of more than 500 "qualified" trusts. As trustee of CIIT, the Bank invested in shares of Penn Central common stock, which upon ultimate sale, gave rise to a pro rata share loss of $23,700 to Hotel Employees, $3,000 to Service Employees, $15,000 to Tugmen, and $40,000 to Dairy Employees. The plaintiffs also seek to maintain this as a class action on behalf of all holders in CIIT units. The remaining substantive allegations in Counts I through 8 are essentially the same as those in 72 C 2551.

The question has been raised whether the entity known as Continental Illinois Investment Trust is amenable to suit. That issue is not being decided at this time, and the question is reserved for further consideration at a later date.

No. 73 C 660

The plaintiffs in this action are the trustees of the Credit Union National Association ("CUNA"). An agreement was entered into with these trustees by which the Bank was appointed an agent with investment discretion as to the purchase and sale of securities. It is alleged that the Bank's investment in Penn Central stock on plaintiff's behalf resulted in a loss to them of approximately $317,000. The plaintiffs also seek to maintain this suit as a class action on behalf of all persons with trust or agency accounts for whom the Bank purchased Penn Central shares. The remaining allegations in this eight-count complaint are similar to those in 72 C 2551, with the exception that the latter four counts are based upon diversity jurisdiction, 28 U. S. C. § 1332.

No. 73 C 772

The plaintiffs, officers of the Air Line Pilots Association, International ("Air Line Pilots") seek to maintain this action on behalf of themselves and also on behalf of the class of all airline pilots presently or formerly in the service of United Airlines ("United") who are beneficiaries of a pension plan established by United for its pilots ("Pension Plan"). ALPA is an unincorporated association organized as a labor organization and has actively represented pilots for purposes of collective bargaining since 1933. The United Pension Plan entered into an agreement appointing the Bank as trustee. Pursuant to its power of discretionary investment under the trust, the Bank purchased Penn Central common stock. The plaintiffs contend generally that Continental failed to disclose that it had substantial commercial loan relationships with Penn Central and that Penn Central was known to the Bank to be in a precarious financial position. The Pension Fund is alleged to have lost approximately $1,500,000 through the Bank's investment in this stock. Similar investments involving common stock of other companies, i.e., MAI, Trans World Airlines ("TWA"),

Lum's, Inc. ("Lum's"), and United States Freight Co. ("Freight Co.") allegedly resulted in a loss to the pension of $5,600,000. The Bank is alleged to have been a substantial creditor of each of these companies at the time it purchased their stock for the Pension Plan. It is further alleged that the Bank failed to disclose to the plaintiffs the detailed financial information regarding these companies and also that as a creditor of the same, a conflict of interest might exist.

All of the five cases discussed above are ordered consolidated, for purposes of discovery only. The question of consolidation for trial is reserved for future consideration.

II.

For this Court to have jurisdiction in most of these matters, the plaintiffs must sufficiently allege a violation of Section 10(b) of the Securities Exchange Act and Rule 10b-5 promulgated thereunder. The defendant contends that these complaints fail to state claims cognizable under the Securities Act and moves for dismissal.

Section 10(b) of the Securities Exchange Act provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange . . . to use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Rule 10b-5 provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of a national securities exchange,

(1) to employ any device, scheme or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

The defendant's first argument is that Section 10(b) does not reach the relationship between trustees and trust beneficiaries, nor does it provide a remedy for breach of contract. Initially this Court must recognize that the mere fact that the plaintiffs are beneficiaries under a trust agreement does not preclude them from bringing an action under § 10(b) for alleged fraud in the purchase or sale of securities on behalf of the trust. Appropriate plaintiffs in a Rule 10b-5 suit are not limited to a "purchaser or seller" of securities, the traditional requirement set out in the decision of *Birnbaum* v. *Newport Steel Corp.*, 193 F. 2d 461 (2d Cir., 1952), *cert. denied*, 343 U. S. 956. The statutory authorization for the rule refers to the prohibition of deceptive devices "for the protection of investors" and the Supreme Court in *Superintendent of Insurance* v. *Bankers Life and Casualty Co.*, 404 U. S. 6, 12-13, stated that the crux of that case was the fact that the plaintiff "suffered injury as a result of deceptive practices touching its sale of securities *as an investor*" (emphasis added). In reliance on this judicial and statutory authority, the Seventh Circuit in *Eason* v. *General Motors Acceptance Corp.*, 490 F. 2d 654 (7th Cir., 1973), expressly discarded the *Birnbaum* rule and extended the statutory protection to a broader class of persons. The emphasis in this circuit now is on "persons who, *in their capacity as investors*, suffer significant injury as a direct consequence of fraud in connection with a securities transaction, even though their participation in the transaction did not involve either the purchase or the sale of a security." (490 F. 2d at 659)

In essence, the defendant would have this Court limit the plaintiffs to such remedies as are locally available to mere beneficiaries of a discretionary trust. However we should not ignore the direction in *Tcherepnin* v. *Knight,* 389 U. S. 332, 336 (1967) that in construing the 1934 Act "form should be disregarded for substance and the emphasis should be on economic reality." In light of this directive, we are compelled to recognize that the defendant is not merely a passive safekeeper of funds but instead is actually an active money manager with whom the plaintiffs have entered into investment agreements, regardless of whether these are otherwise described as trust or agency agreements. Therefore, the plaintiffs may truly be described as "investors" and are thus within the class of persons to be protected by Rule 10b-5.

The next question for our consideration is whether the claims allege merely breaches of contract and fiduciary duty, and as such fail to allege fraud "in connection with the purchase or sale" of a security. First, this Court reads the complaints to allege failure to disclose material information in violation of Rule 10b-5. Whether they also set forth claims for breaches of contract or of fiduciary duty becomes irrelevant. The Supreme Court, in the *Bankers Life* case, made it clear that Federal securities law was appropriate in a fraud situation notwithstanding the availability of a state remedy. 404 U. S. at 12. Secondly, the purpose of Rule 10b-5 is to prohibit all fraudulent schemes in connection with the purchase or sale of a security. *James* v. *Gerber Products Co.,* 483 F. 2d 943 (6th Cir., 1973); *A. T. Brod* v. *Perlow,* 375 F. 2d 393 (2d Cir., 1967). Heeding the caution of *Bankers Life* that § 10(b) be viewed "flexibly, not technically and restrictively", 404 U. S. at 12, this Court deems the defendant's alleged nondisclosure as trustee or agent viz-a-viz the plaintiff as beneficiaries and principals, to fall within the ambit of Federal securities law.

The fraud alleged in *Bankers Life* did not run between purchaser and seller. The rule that this is a requirement of 10b-5

actions, as stated in *Rippey* v. *Denver United States National Bank*, 260 F. Supp. 704, 715 (D. Colo., 1966), cannot any longer be considered to be the law. In *Bankers Life*, both the purchaser and seller of the corporation's stock practiced fraud on the corporation. In permitting the suit, the Supreme Court stated:

> ". . . disregard of trust relationships by those whom the law should regard as fiduciaries, are all a single seamless web" along with manipulation, investor's ignorance and the like.
>
> 404 U. S. at 12, citing H. R. Rep. No. 1383, 73d Cong., 2d Sess., 6

In other contexts, the courts have allowed 10b-5 suits though the fraud did not run from purchaser to seller. In *A. T. Brod & Co.* v. *Perlow, supra*, the fraud ran from a purchaser to his broker, and in *Opper* v. *Hancock Securities Corp.*, 467 F. 2d 157 (2d Cir., 1966) and *Goodman* v. *H. Hentz & Co.*, 265 F. Supp. 440 (N. D. Ill., 1967), the fraud ran from the broker to his client. See also, *Kasner* v. *H. Hentz & Co.*, ¶ 93,819 CCH FED. SEC. L. REP. (5th Cir., 1973). In the corporate setting, derivative suits have been allowed under 10b-5 for fraud perpetrated upon a corporation by its directors. *Ruckle* v. *Roto American Corp.*, 339 F. 2d 24 (2d Cir., 1964); *Schoenbaum* v. *Firstbrook*, 405 F. 2d 200, reviewed en banc, 405 F. 2d 215 (2d Cir., 1968), *cert. denied*, sub. nom., *Manley* v. *Schoenbaum*, 395 U. S. 906 (1969). In the *Ruckle* case, the Court noted:

> "There can be no more effective way to emasculate the policies of the Federal securities laws than to deny relief solely because a fraud was committed by a director rather than an outsider."

Two additional cases which militate for the maintenance of the instant suits in the Federal Courts are *Heyman* v. *Heyman*, 356 F. Supp. 958 (S. D. N. Y., 1973) and *James V. Gerber Products Co.*, 483 F. 2d 944 (6th Cir., 1973), in which the courts

found that the plaintiffs as beneficiaries of trusts had standing to sue their trustees under Rule 10b-5. The defendant Bank endeavors to distinguish the latter case by noting that the trustee and the purchaser of stock were intertwined through an interlocking directorate, whereas the fraud alleged in the instant case is unilateral. We do not feel this is a cogent distinction. On the contrary, the facts in the *James* case seem quite analogous to those in the instant suit. Both involve what are essentially fiduciary breaches and the corporate entanglement in *James* is rather similar to the complex commercial involvement the Bank is alleged herein to have had. Therefore, there may be Federal securities fraud regardless of whether the means to accomplish it is unilateral or involves a third-party buyer or seller.

The second major argument advanced by the defendant is that the Federal regulatory scheme governing banks, vests in the Comptroller of the Currency, under the National Banking Act, 12 U. S. C. § 1, et seq., rather than the Securities and Exchange Commission, authority to regulate national banks in the performance of their banking functions. Defendant reasons, therefore, that the "conflicts" alleged in these cases are within the exclusive jurisdiction of the Comptroller.

The Securities Act of 1933 expressly exempts from registration:

> ". . . any security issued or guaranteed by any bank; * * * or any interest or participation in any common trust fund or similar fund maintained by a bank exclusively for the collective investment and reinvestment of assets contributed thereto by such bank in its capacity as trustee * * *."
>
> 15 U. S. C. § 77c

The Securities Exchange Act of 1934 exempts from its registration requirements:

> ". . . any interest or participation in any collective trust funds maintained by a bank * * * which interest or participation is issued in accordance with (i) a stock-bonus, pension, or profit-sharing plan which meets the

requirements for qualification under Section 401 of Title 26 * * *."

15 U. S. C. § 781

The 1934 Act further provides:

"In respect of any securities issued by banks the deposits of which are insured in accordance with the Federal Deposit Insurance Act, the powers, functions and duties vested in the Commission under this chapter to administer and enforce Section 781 (registration), 78m (reports), 78n(a) and (c) (proxies), 78n(d) and (f) (tender offers) and 78p (insider trading) of this title with respect to national banks * * * are vested in the Comptroller of the Currency * * *."

15 U. S. C. § 781(i)

This Court held in *Brackett* v. *Vose*, No. 72 C 2843, (N. D. Ill., Nov. 27, 1973), that the former two provisions exempt interests in non-business trusts from registration, but do not concomitantly free the trustees dealing on behalf of those trusts from the scope of the anti-fraud provisions of the 1933 and 1934 Acts. Also illuminating are the decisions in *Lehigh Valley Trust Co.* v. *Central National Bank of Jacksonville*, 409 F. 2d 989 (4th Cir., 1969) and *Carrol* v. *First National Bank of Lincolnwood*, 413 F. 2d 353, 358 (7th Cir., 1969), which held national banks liable under the Federal securities law. In *Lehigh*, the Court noted:

"[t]he fact that Congress exempted from the registration requirements of the Securities Act of 1933 the securities of any 'banking institution * * * the business of which is substantially confined to banking and is supervised by the State * * * banking commission * * *' (15 U. S. C. § 17(a)(2), indicates that Congress was aware of the peculiar problems and strengths of banks resulting from their regulation by state and Federal banking statutes. *That Congress made no express general exemption for banks under the fraud provisions of either the Securities Act of 1933 or the Securities Exchange Act of 1934 indicates that Congress did not intend any such exemption.*" (emphasis added)

Furthermore, in *Affiliated Ute Citizens* v. *U. S.*, 406 U. S. 128 (1972), the Supreme Court expressly held a national bank liable under 10b-5.

Additionally, the defendant attempts to infer an exemption from the broad reaches of the Federal securities law for national banks when acting as trustees, by virtue of the delegation to the Comptroller of extensive authority to regulate the trust activities of the national banks, with particular reference to potential conflicts of interest which may arise during the conduct of its fiduciary duties. Pursuant to that authority, the Comptroller has adopted the following regulation to eliminate such conflicts:

> "Self Dealing . . .[F]unds held by a national bank as fiduciary shall not be invested in stock or obligations of or property acquired from, the bank or its directors, officers or employees, or individuals with whom there exists such a connection, *or organizations in which there exists such an interest as might affect the exercise of the best judgment* of the bank in acquiring the property. . . ." (emphasis added)

12 C. F. R. 9.12

Through the Financial Institutions Supervisory Act of 1966, 12 U. S. C. § 1818, Congress gave the Comptroller the added power to formally adjudicate any violations of its regulations. However, the Court in *Blaney* v. *Florida National Bank at Orlando*, 357 F. 2d 27 (5th Cir., 1966), seriously questioned whether the national trust regulations were motivated by the broad remedial purposes underlying the Securities Exchange Act and noted that instead:

> ". . . they were primarily designed, rather, to place national banks on an equal competitive basis with state banks and trust companies in the state where the national bank is situated."

357 F. 2d at 30.

Therefore just as Section 12(i) of the 1934 Act, 15 U. S. C. § 781(i) while vesting in the Comptroller authority over various

aspects of the issuance of securities by certain banks does not free the transactions in these securities from the anti-fraud provisions, national banks when acting as trustees are equally subject to such liability.

The defendant also cites *Ricci* v. *Chicago Mercantile Exchange*, 409 U. S. 289 (1973) and *Chicago Mercantile Exchange* v. *Deaktor*, ... U. S. ....., 38 L. Ed. 2d 344 (1973), for the proposition that the Comptroller has exclusive authority over bank conflicts of interest. A reading of the opinions in these cases, however, discloses that they deal with the concept of "primary jurisdiction." The defendant has conceded that this doctrine is inapplicable to the 10b-5 claims. We agree. A predicate to application of the doctrine of primary jurisdiction is an inherent incompatibility between two regulatory schemes. Regulation by one Federal agency does not automatically immunize an industry from regulation by another Federal agency; nor are concurrent state and Federal regulation of an industry mutually repugnant. *Tcherepnin* v. *Knight*, 389 U. S. (1967); *SEC* v. *National Securities, Inc.*, 393 U. S. 453 (1969); *California* v. *Federal Power Comm.*, 369 U. S. 482, 489 (1962). Under scrutiny in *Ricci, supra*, was the Commodities Exchange Act, 7 U. S. C. § 1 et seq., which by its very nature has certain anti-competitive aspects. Thus, there was the necessary "incompatibility" between that Act and the anti-trust laws. Such an "incompatibility" does not exist between the securities laws and the national banking laws. Repeal of the securities laws is not "necessary to make the [National Banking Act] work. . . ." *Silver* v. *New York Stock Exchange*, 373 U. S. 341, 357 (1963); *Ricci* v. *Chicago Mercantile Exchange*, 409 U. S. at 301. But even if there were an "incompatibility" between the two, it is axiomatic that the Court must first attempt to reconcile the operations of the coexisting schemes rather than to hold one is completely ousted of jurisdiction. *Silver* v. *New York Stock Exchange*, 373 U. S. at 357-58; *Thill Securities Corp.* v. *New York Stock Exchange*, 433 F. 2d 264, 268 (7th Cir.,

1970). Finally, even if the doctrine of primary jurisdiction were applicable to these facts, the solution to the problem would not be for the Court to order dismissal, but instead to stay the proceedings "until the administrative officials have had an opportunity to act." *Ricci* v. *Chicago Mercantile Exchange, supra; Carnation Co.* v. *Pacific Westbound Conference,* 383 U. S. 213 (1966).

Besides the failure to disclose information regarding the financial condition of the issuers and the defendant's alleged conflict of interest, the various counts in Cause No. 73 C 772 also assert a failure to disclose violation of the Comptroller's Regulation 12 C. F. R. 9.12. In *Blaney, supra,* the Court expressly held that the national trust regulations were not designed to create a private civil remedy. The plaintiffs cannot circumvent this holding by grafting an alleged violation of the trust regulations onto a 10b-5 failure to disclose allegation and expect to recover on that basis. The 10b-5 fraud must stand or fall on its own, irrespective of a concurrent violation of the banking regulations. Therefore, to the extent Cause No. 73 C 772 attemps to state a claim for relief on the basis of 12 C. F. R. 9.12, it must be dismissed.

The defendant's third major argument asserts that Counts II and III in Causes 72 C 2551, 72 C 2935, 73 C 46, and 73 C 660 merely allege negligence, imprudence, want of due care, and nonsuitability and as such fail to allege a sufficient § 10(b) claim. The cases indicate that § 10b-5 contemplates something more than mere negligence, imprudence or error in judgment. See *Mercury Investment Co.* v. *A. G. Edwards & Sons,* 295 F. Supp. 1160 (S. D. Tex., 1969): *Hecht* v. *Harris, Upham & Co.,* 283 F. Supp. 417 (N. D. Cal., 1968); *Colonial Realty Corp.* v. *Bache & Co.,* 358 F. Supp. 178 (2d Cir., 1966). However, the thrust of these counts is not that defendant was imprudent in selecting these investments, but that it concealed material information in so doing, namely, that the issuer of the securities had insufficient cash, substantial and accelerating

operating losses, debt service requirements in excess of cash generated, and inflated market price. Each count alleged that defendant "knew or should have known" the facts concealed. This is all that the rule requires, as was held in *Heit* v. *Weitzen*, 402 F. 2d 909, 914 (2d Cir., 1968):

> ". . . we pass only upon the legal sufficiency of the complaints to allege a claim for relief. This each of the complaints fairly does. The charge that defendants 'knew or should have known' adequately alleges actual knowledge of the falsity of the statements, and alternatively, negligence or lack of diligence in failing to ascertain the true facts. If some form of scienter test is to be applied, as Judge Friendly seems to suggest in his concurring opinion in *Texas Gulf Sulphur*, we think the alternative allegation of actual knowledge of falsity is amply sufficient as a matter of pleading. And this would seem to be so whether the scienter test ultimately applied be strict or liberal. . . ."

In any case, the Federal Rules of Civil Procedure merely require "a short and plain statement of the claim." Rule 8, F. R. C. P. Thus, as long as the defendant is given notice of the nature of the claim, the complaint cannot be dismissed, specifically and exactitude of pleading are no longer required. See *Conley* v. *Gibson*, 355 U. S. 41 (1957). Secondly, any inferences drawn must be favorable to the plaintiff. *United Milk Products Co.* v. *Michigan Ave. National Bank of Chicago*, 401 F. 2d 14, 17 (7th Cir., 1968). The two counts in question should not be dismissed at this time.

Therefore, for the above reasons, these plaintiffs may bring this action against the defendant as trustee and investment agent for violation of Rule 10b-5; and the defendant's several motions to dismiss the 10b-5 claims in the cases captioned above are denied, except to the limited extent granted above in Cause No. 73 C 660.

III.

Motion to Dismiss Counts V and VIII of Cause No. 73 C 660

The defendant argues that the state law Counts V and VIII in Cause No. 73 C 660 in essence assert "intra-bank" conflicts of interest and, as such, are subject to the "exclusive primary" jurisdiction of the Comptroller of the Currency. The arguments made in support of this motion to dismiss are basically indistinguishable from those previously advanced regarding "exclusive" jurisdiction as to the Federal claims. Thus we adopt the reasons for denying that portion of the motion and conclude that the doctrine of "primary jurisdiction" is equally inapposite to these counts. This position is reinforced by a perusal of 12 U. S. C. § 92a, which makes the right of national banks to act as trustees and in other fiduciary capacities turn upon the law of the state in which the national bank is located. Thus a national bank, when acting as trustee, cannot escape the purview of the state law of trusts and contracts. For these reasons, defendant's motion to dismiss Counts V and VII is denied.

IV.

Motion to Dismiss the Alleged Violations of § 17a of the Securities Act of 1933 in Cause No. 73 C 772

Counts I, III and V of the Air Line Pilots' complaint allege violations of § 17(a) of the Securities Act of 1933, in addition to the violation of § 10b and Rule 10b-5 of the 1934 Act. The defendant has moved to dismiss these counts for the same reasons advanced as to the § 10(b) claims, but also on the basis that § 17(a) does not create a private right of action for damages.

Section 17(a) of the Act provides:

> (a) It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instru-

ments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

This provision is clearly criminal in nature and does not explicitly provide a civil remedy. Any private right of action under this section can only be implied through application of "the general principle of tort law that violation of a provision of a criminal statute can, unless expressly or impliedly negatived by the statute itself, give rise to a civil remedy in tort." *Trussell* v. *United Underwriters, Ltd.*, 228 F. Supp. 757, 765 (D. Colo., 1964); cf. Restatement, Second, Torts, § 286. Various courts have expressly recognized the existence of such a remedy, while others have simply assumed, without actually deciding the question, that a private cause of action is present under § 17(a). See, *Globus* v. *Law Research Service, Inc.*, 418 F. 2d 1276, 1283 (2d Cir., 1969), *cert. denied*, 397 U. S. 913 (1970); *Dyer v. Eastern Trust and Banking Co.*, 336 F. Supp. 890, 903 (D. Me., 1971); *Dorfman* v. *First Boston Corp.*, 336 F. Supp. 1089 (E. D. Penn., 1972). This position has not met with complete jural concurrence; some courts have denied this private civil remedy. See, *Dyer* v. *Eastern Trust and Banking Co.*, 336 F. Supp. at 904; 6 Loss, Securities Regulation 3912 (1969). In the Seventh Circuit, the question does not appear to have been completely resolved, see, *Surowitz* v. *Hilton Hotels Corp.*, 342 F. 2d 596, 604 (7th Cir., 1965), although one district court has

twice flatly held that this private action is available. *Freed* v. *Szabo Food Service, Inc.*, CCH Fed. Sec. L. Rep. § 91,317 (N. D. Ill., 1964); *Schaefer* v. *First National Bank of Lincolnwood*, 326 F. Supp. 1186, 1190 (N. D. Ill., 1970). Even though the preponderance of authority seems to weigh heavily in favor of permitting a private remedy under § 17(a), it is unnecessary for the Court to resolve this conflict for the purposes of the present suit. In this opinion, we have previously allowed the § 10(b) claims to stand. Thus, the better approach is that taken by the *Globus* court when it adopted the view set forth by Judge Friendly, in his concurring opinion in *S. E. C.* v. *Texas Gulf Sulphur Co.*, 401 F. 2d 833, 864 (2d Cir., 1968): there seems to be little practical value in denying the existence of a private action under § 17 once it is established that a plaintiff has an action under § 10(b) of the 1934 Act. Therefore, the Air Line Pilots may assert a private remedy under § 17(a).

There is a motion filed with this Court to dismiss Counts IX through XIII in Cause No. 73 C 772 for lack of pendent or diversity jurisdiction. Since this Court has previously decided that a valid 10(b) claim exists in the prior counts of this cause, there is pendent jurisdiction for the related state law claims. Thus, the defendant's motion to dismiss these counts must be denied.

In summation, the motions to dismiss the 10b-5 claims in Cause Nos. 72 C 2551, 72 C 2935, 73 C 46 and 73 C 772 are denied; the motion to dismiss the 10b-5 claims in No. 73 C 660 are granted in part and denied in part; the motion to dismiss Counts V and VIII in Cause No. 73 C 660 is denied; the motion to dismiss the alleged violations of § 17(a) of the 1933 Act in Counts I, III and V of Cause No. 73 C 772 is denied; the motion to dismiss Counts IX through XIII in Cause No. 73 C 772 is denied; the motion to consolidate the various causes is granted for purposes of discovery only. The motion to dismiss as to CIIT in Cause No. 73 C 46 is stayed, pending further briefing.